



TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

Release Number: **201131025**

Release Date: 8/5/2011

Date: May 13, 2011

501.03-30

501.03-08

501.33-00

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:

Tax Years:

Dear

This is our final determination that you do not qualify for exemption from Federal income tax under Internal Revenue Code section 501(a) as an organization described in Code section 501(c)(3).

Because you do not qualify for exemption as an organization described in Code section 501(c)(3), donors may not deduct contributions to you under Code section 170. You must file Federal income tax returns on the form and for the years listed above within 30 days of this letter, unless you request an extension of time to file. File the returns in accordance with their instructions, and do not send them to this office. Failure to file the returns timely may result in a penalty.

We will make this letter and our proposed adverse determination letter available for public inspection under Code section 6110, after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in Notice 437. If you agree with our deletions, you do not need to take any further action.

If you have any questions about this letter, please contact the person whose name and telephone number are shown in the heading of this letter. If you have any questions about your Federal income tax status and responsibilities, please contact IRS Customer Service at

1-800-829-1040 or the IRS Customer Service number for businesses, 1-800-829-4933. The IRS Customer Service number for people with hearing impairments is 1-800-829-4059.

Sincerely,

Lois G. Lerner  
Director, Exempt Organizations

Enclosure  
Notice 437  
Redacted Proposed Adverse Determination Letter



TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

**DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224**

Date: March 3, 2011

Contact Person:

Identification Number:

501.03-30

Contact Number:

501.03-08

501.33-00

FAX Number:

Employer Identification Number:

Dear

We have considered your application for recognition of exemption from Federal income tax under section 501(a) of the Internal Revenue Code ("Code"). Based on the information provided, we have concluded that you do not qualify for exemption under section 501(c)(3). The basis for our conclusion is set forth below.

Facts

You are a nonprofit membership corporation under state law. Your Articles of Incorporation state that you are organized exclusively for charitable and educational purposes and to relieve the burdens of government, either directly indirectly or by contributions to organizations that qualify as exempt under section 501(c)(3) of the Code. Your Articles also state that you will carry out this purpose by providing educational materials and classroom supplies to teachers to be used for instruction of their students.

Your Board of Directors is comprised of three persons. One Director serves as your President and Treasurer, and his wife serves as both Vice President and Secretary. You presently have one unpaid volunteer employee and no paid employees. You have adopted a Conflicts of Interest Policy, and you state that if you hire employees or pay compensation, you will comply with the prohibitions described in this policy.

You operate an on-line registry for teachers, who can register on your website and list educational materials and supplies that are needed for their classrooms. Teachers may add or remove items from their registry. A donor can go to the website, search for a particular teacher's registry, and either select items that the donor would like to purchase for the teacher or purchase gift certificates the teacher may redeem through the website. When an item is selected for purchase, the order is sent electronically to a specific vendor, who ships the item at the expense of the donor, directly to the teacher at their school. Once an item is selected for purchase, the item is automatically removed from the teacher's registry. The donors contribute amounts equal to the retail prices of the selected items and you purchase the items from the vendor at wholesale prices.

Currently, you have contracts with one supply company and one marketing company, both of whom are unrelated to you, to provide goods and services. You also have a Representative Agreement with your state's Parents and Teachers Association which promotes you in exchange for two percent of your gross donations from the donors within the state.

Each teacher who registers to receive classroom supplies agrees that the items received will be used only within the classroom and for the benefit of the students in the class identified in their profile and school registry. Each teacher also agrees not to use any item received for personal or private purposes, and if the teacher is unable to use an item, it will be returned to you or used for another educational purpose.

The software you use to operate your website was originally owned by a company founded by your President. You paid all the costs associated with developing the software and this company transferred to you all ownership rights to the software. You own all the trademarks, service marks, and trade names associated with your software and your activities. You do not plan to license or sell these items.

Your primary source of revenue will be from the contributions made by the public when they purchase school materials, supplies, or gift cards through your website for registered teachers. Due to your lack of funds while exempt status has been pending, your President has expended funds on your behalf. As a result, you have entered into a loan agreement to repay the principal amounts borrowed, exclusive of interest.

### Law

Section 501(c)(3) of the Code describes organizations organized and operated exclusively for charitable, scientific, or educational purposes.

Section 1.501(c)(3)-1(a) of the Income Tax Regulations states that in order to be described in section 501(c)(3) of the Code, an organization must be both organized and operated for one or more of the purposes specified in that section. If an organization fails to meet either the organizational or operation test, it is not described in section 501(c)(3).

Section 1.501(c)(3)-1(c)(1) of the regulations states that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of the exempt purposes specified in section 501(c)(3) of the Code. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(1)(i) of the regulations describes various exempt purposes, including "educational."

Section 1.501(c)(3)-1(d)(3)(i) of the regulations defines "educational" as:

- (a) The instruction or training of the individual for the purpose of improving or developing his capabilities; or*

*(b) The instruction of the public on subjects useful to the individual and beneficial to the community.*

Rev. Rul. 54-305, 1954-2 C.B. 127, describes an organization whose primary purpose is the operation and maintenance of a purchasing agency for the benefit of its otherwise unrelated members that are exempt as charitable organizations. The organization in this revenue ruling did not qualify for exemption under the predecessor to section 501(c)(3) of the Code because its activities consisted primarily of the purchase of supplies and the performance of other related services, which are considered an ordinary trade or business.

Rev. Rul. 64-274, 1964-2 C.B. 141, involves an organization that provides assistance to worthy and needy students by making available to them: (1) financial gifts, grants, awards, scholarships, fellowships, prizes, interest-free loans, and subsidies; (2) free housing; and (3) books and instructional supplies or equipment. The students selected are those with exceptional records of scholastic achievement but who, because of lack of funds, could not otherwise attend a college or university. The revenue ruling concludes that the organization is engaged in activities to aid students in attaining an education, and therefore are charitable within the meaning of the regulations.

Rev. Rul. 72-369, 1972-2 C.B. 245, involves an organization formed to provide managerial and consulting services at cost to unrelated exempt organizations. This revenue ruling held that providing managerial and consulting services on a regular basis for a fee is a trade or business ordinarily carried on for profit. Merely because the services were provided at cost and solely for exempt organizations was not sufficient to characterize this activity as charitable within the meaning of section 501(c)(3) of the Code. Furnishing the services at cost lacks the donative element necessary to establish the activity as charitable.

In Rev. Rul. 76-442, 1976-2 C.B. 148, an organization's primary activity is the offering of free legal services for personal tax and estate planning to individuals who wish to make current and deferred gifts to charity as part of their overall tax and estate planning. The revenue ruling stated that aiding individuals in their tax and estate planning is not a charitable activity in the generally accepted legal sense. The organization is providing commercially available services to individuals who can afford them. The revenue ruling concludes that although funds may ultimately be made available to charity as a result of the organization's planning assistance to individuals, the benefits to the public are tenuous in view of the predominantly private purpose served by arranging individuals' tax and estate plans. The fact that gifts to charity are contemplated in the plans does not convert the organization's assistance into a charitable activity or one that promotes social welfare within the meaning of the regulations.

In Easter House v. U.S. 12 Cl. Ct. 476 (1987), aff'd in an unpub. opinion, 846 F. 2d 78 (Fed. Cir. 1988), cert. den., 488 U.S. 907 (1988), the organization, in exchange for a fee, provided adoption services to parents seeking to adopt a child, including services to pregnant women who intended to place their newborns for adoption. These fees were the organization's sole source of income. The Claims Court concluded that the organization's business purpose of operating an adoption service, not the advancement of educational and charitable activities, was its primary goal. It competed with other commercial organizations providing similar services. Thus, "[p]laintiff's competition provides its activities with a commercial hue." 12 Cl. Ct. at 486. Accordingly, the organization did not qualify for exemption under section 501(c)(3) of the Code.

In Airlie Foundation v. I.R.S., 283 F.Supp. 2d 58 (D.D.C. 2003), the District Court found that the organization was formed principally to organize, host, conduct, and sponsor educational and other charitable functions on its facilities. The organization's patrons were not limited to tax-exempt entities, but included patrons of a private and corporate nature. The organization paid advertising and promotional expenses and derived substantial income from weddings and special events held at its conference center. The court determined that the organization's activities competed with a number of commercial, as well as non-commercial entities, which strongly evidenced a commercial nature and purpose. The court concluded that although the organization carried out a number of charitable and educational activities, these were incidental to its primary activity of operating a for-profit conference center. The court stated, "While plaintiff's organizational purpose is exempt and the foundation operates, in important respects, in an exempt fashion, there is a distinctive "commercial hue" to the way Airlie carries out its business. Id. at 65.

### Analysis

An organization will be regarded as operated exclusively for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of the exempt purposes specified in section 501(c)(3) of the Code. Section 1.501(c)(3)-1(c)(1) of the regulations. One such exempt purpose is the advancement of education. Section 1.501(c)(3)-1(d)(1)(i). The term "educational" for purpose of the regulations is defined as including the instruction or training of individuals and the instruction of the public. Section 1.501(c)(3)-1(d)(3)(i).

By facilitating the donation, purchase and delivery of educational materials and classroom supplies to teachers who have expressed a need for these items and who will use them in the instruction of their students, you are, in essence, providing commercial fundraising services to the schools. These activities do not constitute furthering "education" within the meaning of the regulations. Instead, your services are similar to a commercial vendor of educational products or services that provides fundraising assistance to charitable organizations.

You are similar to the organization described in Rev. Rul. 54-305, supra, which did not qualify for exemption under section 501(c)(3) of the Code. By enabling donors to purchase school supplies and equipment for teachers who need these items for educational purposes, you are providing purchasing services for the schools. You are also similar to the non-qualifying organization in Rev. Rul. 72-369, supra, because you enable donors to donate these items based on their retail price but you purchase the items at wholesale, similar to a commercial enterprise carried on for profit. In addition, you are similar to the non-qualifying organizations in Easter House v. U.S., supra, and Airlie Foundation v. I.R.S., supra, which were determined to be carrying on essentially commercial activities, rather than activities that furthered a charitable purpose.

By providing donors with a simple and convenient method by which they can easily donate needed school supplies and educational materials to teachers who have requested them, you are similar to the organization in Rev. Rul. 76-442, supra, which concluded that the organization's activities were themselves not charitable activities, but constituted the provision of commercially available services to individual donors.



However, you are unlike the qualifying organization described in Rev. Rul. 64-274, supra, because you are not providing educational supplies or classroom supplies to needy students. Instead, your activities merely facilitate donors providing these items to the schools that need them.

Upon consideration of all the facts and circumstances, we conclude that your primary purpose is not "educational" within the meaning of section 1.501(c)(3)-1(d)(i) of the regulations. Instead more than an insubstantial part of your activities is in furtherance of a non-exempt commercial purpose. Section 1.501(c)(3)-1(c)(1) of the regulations.

As a result, you are not organized and operated exclusively for exempt purposes within the meaning of section 501(c)(3) of the Code. Therefore, you do not qualify for exemption as an organization described in section 501(c)(3) and you must file federal tax returns. Furthermore, contributions to you are not deductible under section 170 of the Code.

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning. You must submit the statement, signed by one of your officers, within 30 days from the date of this letter. We will consider your statement and decide if the information affects our determination.

Your protest statement should be accompanied by the following declaration:

*Under penalties of perjury, I declare that I have examined this protest statement, including accompanying documents, and, to the best of my knowledge and belief, the statement contains all the relevant facts, and such facts are true, correct, and complete.*

You also have a right to request a conference to discuss your protest. This request should be made when you file your protest statement. An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you. If you want representation during the conference procedures, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. For more information about representation, see Publication 947, *Practice before the IRS and Power of Attorney*. All forms and publications mentioned in this letter can be found at [www.irs.gov](http://www.irs.gov), Forms and Publications.

If you do not file a protest within 30 days, you will not be able to file a suit for declaratory judgment in court because the Internal Revenue Service (IRS) will consider the failure to protest as a failure to exhaust available administrative remedies. Code section 7428(b)(2) provides, in part, that a declaratory judgment or decree shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted all of the administrative remedies available to it within the IRS.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848 and any supporting documents to this address:

Internal Revenue Service  
TE/GE SE:T:EO:RA:T:1

1111 Constitution Ave, N.W.  
Washington, DC 20224

You may also fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

Robert Choi  
Director, Exempt Organizations  
Rulings & Agreements